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Keynes' monetary theory and transition economies*

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Abstract

After a short outline of how Keynes' monetary theory was being accepted, read and discussed before the transition period started at early 1990s, two key issues somehow connected with Keynes are being analyzed in this paper. The first issue focuses on the problems of selling of business enterprises, i.e.their shares, in transition countries, as they had to be transformed from stately or socially owned to privately owned companies. These problems are remotely similar to problems resolved or 'resolved' by the Say's Law. If the government does not enable private sector to buy companies, domestic savings and capital formation will decrease. For instance, what the government should have done in cases where business enterprises were socially owned is being analyzed and illustrated with IS-LM diagrams for the open economy. The second issue deals with how the central bank should behave – especially if the government had not done anything to enable smooth purchases of business enterprises by the domestic private sectors. The central bank should prevent either monetary expansion or appreciation of the domestic currency by sterilized purchases of the surpluses of foreign currencies on the foreign exchange market. Both issues are somehow connected with Keynes and/or economists whether either his followers or not.

Key words: *Monetary theory, Keynes, transitional economies, IS-LM diagram*

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1. Introduction

Before addressing the topic outlined in the title of this paper, some words of introduction. In the former Yugoslavia Keynes was not discussed only in the context of his economic theories, and hence we start by presenting the perception of Keynes in the former Yugoslavia. Next, we are interested in what Keynes' contribution to monetary economy. This brings us to the IS-LM model or the Hicks-Hansen diagram and problems related to it. In an open economy, and small economies cannot be closed, the diagram needs to be modified. A further modification is needed because central banks are not any more interested in the quantity of money, particularly in the narrow money, but in interest rates. All these parts of the text, of course, lead to the main issue of the paper, Keynes' monetary theory for transition countries.

Of course Keynes is not only or primarily the IS-LM diagram, but we try to establish whether this diagram can help explaining the developments in transition economies as the consequence of the unavoidable, without which the transition could not have started. This was privatisation, or in the context of the former Yugoslavia, the abolition of social ownership of non-financial enterprises. The question is, of course, how it was done. O. Blanchard (Blanchard, 1997, p. 118), for example, illustrated using the IS-LM diagram mistakes made by Germany, its monetary policy and exchange rate policy, at the time of reunification[2]. In our case, the issue is not reunification or privatisation, but, as we had social ownership of non-financial enterprises, the abolition of social ownership.

2. Keynes in the former Yugoslavia before transition

Leaving aside papers and books criticising Keynes as a bourgeois economist, as he was not a Marxist nor was he in favour of worker's self management, we need to mention a book published in 1938 by J. Tomašević, who quotes Keynes several times (Tomašević, 2004). After World War II, if we skip the first decade or so, for me and probably for some other colleagues the first texts by Keynes were his two books on money (Keynes, 1950, and Keynes 1950a), which were published in 1930. Today these books remain important. The General Theory was translated, and the original text was not available (Keynes, 1953). Because of the translation, the book was less appealing. Books on money were available in original and therefore more appealing. I got acquainted with the General Theory, probably as many others, through Hansen's books (Hansen, 1949, and Hansen, 1953).

[2] Germany's compensated its expansionary fiscal policy with a restrictive monetary policy. Interest rates were increased, which lead to problems of other countries within the ERM system. The currency should have revaluated.

Books on money were interesting for someone who was studying money, but there is more to it. In the first book we can, for example, find his two fundamental equations on the value of money ("fundamental equations"). Even though they represent a truism, which is confirmed by Keynes (Keynes, 1950, p. 138), they present interesting, important and possible relationships among different macroeconomic aggregates and prices of consumer goods, i.e. the value of money, expressed as its purchasing power.

From these equations one can derive, among other things, that an increase of investments increases the share of profit, or if we talk about workers and capitalists, capitalists by investing enable financing of large investments because their profits increase accordingly. The problem is investments and not the financing of investments, which was adopted by N. Kaldor (Kaldor, 1960)[3] and others. J. Pokorn was interested in the substance of the price of consumer goods (Pokorn, 1961, and Pokorn 1967).

At least in Ljubljana students were in the course on money first taught the formation of the national income ("income determination") and the IS-LM diagram. The course on money historically starts with studying the main macroeconomic problem of the time, i.e. the general level of prices. The same course in the former Yugoslavia after World War II had first to accommodate other macroeconomic problems. Macroeconomics was accepted as an independent science relatively late, also because one cannot, for instance, get back to Marx, who was one of the first macroeconomists, but he never used the word. We are interested, of course, in money.

3. Keynes' monetary theory, IS and LM curves, IS-LM diagram

Let's us leave aside the fact that after the war all economist were Keynesians, who than in the 70s almost disappeared – similar to Marxists at the beginning of transition in the former Yugoslavia. Although there exists a difference between Keynes and Keynesians (Leijonhufvud, 1968), as well as between Marx and Marxists, we are not primarily interested in quarrels among different groups of economists. By default each group offers something new, but in reality there is little really new. We are interested in Keynes' importance for the monetary theory in the context of transition countries.

Besides monetary theory, Keynes' other contributions are, for instance, the consumption function, the concept of effective demand, then the hypothesis that workers negotiate minimum wage, the existence of involuntary unemployment, difference between savings (S) and investments (I), to name only a few (Greenwald and Sti-

[3] His paper "Alternative Theories of Distribution" analyses Keynes' theory of distribution, even though, as Kaldor indicates, Keynes was never interested in the issue of distribution.

glitz, 1987; King, 2003). If we stay within the topic of money, his key contribution is that more money is held than needed for transactions. The money held in excess of the transaction money is the so called speculative money. Its quantity depends on the difference between the expected and the current interest rate. If we assume constant expectations, its quantity depends on the current interest rate. He explained why it is perfectly rational if people hold their assets in the form of money, which does not generate any return, instead in financial investments, which bring interest revenue.

This inactive money ("idle balances") is a form of assets (financial assets), and also the transaction money, of course, is a form of assets where transaction costs matter. The alternative form of assets is liquid financial assets, for example government securities. All other things equal, an increase in interest rates results in an increase of transaction costs and a decrease in the quantity of inactive money or money as an asset. This brings us to the interest rate as the second variable, which influences money demand. The first variable is the national income. Money demand for transaction purposes depends on the volume of transactions. National income reflects the volume of transactions. If national income increases, the volume of transactions and also the demand for money for transactions increase. This was established already by the followers of the quantitative theory of money.

The quantitative or classic theory of money, according to which an additional quantity of money triggers an increase of aggregate demand and consequently prices and/or, according to the new version, nominal national income (Gordon, 1970)[4], does not know inactive money, which can be activated by increase in the interest rate. In contrast to this theory, according to Keynes an additional quantity of money, if it causes a fall in interest rates, can lead to an increase in the quantity of inactive money and to a relatively small increase in aggregate demand. In an extreme case, i.e. in the case of the so called absolute liquidity preference, which occurs at low interest rates, all additional money becomes inactive money. It gets trapped in the so called liquidity trap and there is no increase in national income.

The demand for money depends on two variables: the interest rate and the national income. If we know the quantity of money and the demand for transaction money, we cannot know at which price level (or nominal national income) is the monetary equilibrium. This brings us to the LM curve in the IS-LM diagram or in the Hicks-Hansen diagram, which has national income (Y) on the y-axis and the interest rate level (i) on the x-axis. The curve runs from the left lower corner of the diagram to the right upper corner. We get to the IS curve, i.e. the curve which shows combinations between national income and interest rates, and where we have an ex-ante or planned equilibrium between investments (I) and savings (S), on the basis of the

[4] Article by Milton Friedman: 'A Theoretical Framework for Monetary Analysis', published in this book.

goods demand and supply curves, or the savings curve, which depends on the national income, and the investments curve, which depends on the interest rate. This curve runs from the upper left corner towards the lower right corner.

The IS and LM curves and the IS-LM diagram cannot be found with Keynes. The first to draw this diagram was J. Hicks (Hicks, 1957)[5] right after Keynes' book was published in 1937. Hicks could do this because, as he pointed out, he had already had the idea behind the diagram and had put it to paper in his other texts. Later he was not that satisfied with the diagram (Hicks, 1980). The diagram can still be found in most textbooks on macroeconomics, although there has been constant critique of it, including several simplifications. A. Leijonhufvud writes, for example, that the IS-LM model is a completely inadequate interpretation of Keynes (Leijonhufvud, 1967, p. 401). According to D. Romer (Romer, 2000), the essence of the model can be expressed without the LM curve.

The IS-LM diagram is, of course, a simplification. It reflects the short term, for example around one year, even though Hicks defined short term as one week. The assumptions are a constant and exogenous quantity of money, and the money demand depends on variables Y and i. Investments depend on the interest rate level, and savings on the national income. The relationship between Y and I, and S, I and money quantity (M) and money demand (L) are constant. This brings us, however, to different problems. As I and S are flows, M and L are stocks, and a variable reflecting the general price level does not exist, definitions of money can be very different.

Ultimately, the IS-LM diagram is only a framework showing relationships between variables of the diagram, which can be used by Keynesians as well as by their rivals, for example the monetarists in the 70s and 80s. Each of the two curves can have a different slope, stability and reactions, i.e. the intensity of moving around in the diagram.

It is generally accepted that Keynes assumed a relatively low elasticity of the IS curve. This can be related to his view that the IS curve reflects change in investments or often the so-called "animal spirit". Elasticity of the LM curve is high. Small changes in interest rate have large impact on money demand. This leads to the conclusion of high efficiency of fiscal policy. Moving the IS curve to the right at times of expansive fiscal policy has a big effect on the economic activity and on the national income. In contrast, the efficiency of monetary policy is relatively small due to low elasticity of the IS curve. From this point we can easily arrive at Keynes seeing monetary policy completely inefficient, with the LM curve being horizontal and fiscal policy fully efficient, with a vertical IS curve.

[5] Famous article "Mr. Keynes and the 'Classics' ", published in Econometrics.

This brings us to the IS-LM diagram being useful for everyone or no one. Differences among them are an empirical question[6], and consequently we need to draw different IS and LM lines.

If investments do not depend very much on the interest rate level, then the IS curve moves close to the vertical position, and vice-versa. If, for example, money demand does not depend significantly on interest rates, then the LM curve moves towards the vertical position, and again vice-versa. The issue is not only how to draw the two curves but, even more importantly, if the curves are stable. For the IS curve it is important if it moves only because of a change in the fiscal policy, and for the LM curve if it moves only because of a change in the monetary policy. The IS curve is unstable if the propensity to consumption (or savings) changes without reason, or the propensity to investments. The LM curve is unstable if changes in money demand cannot be explained.

Besides the perception that the IS-LM diagram is useful for different schools of thought there is the view that Keynes' legacy is something else and therefore it cannot and may not be reduced to this diagram. With this diagram one ignores the destiny of Keynes. J. Robinson, according to (Minski, 1986, p. 103), called it the "bastard" diagram. Besides Robinson and Minsky, other followers of Keynes are Davidson (Davidson, 1972), V. Chick (Chick, 1983), S. Weintraub (Weintraub, 1971), naming only some of them. They are right that Keynes is more than that and that his ideas cannot be captured by merely one diagram. If we stay with the diagram because of the simplicity of presenting some key relations among economic variables we are interested in, then we cannot accept the view that Keynes only had in mind a vertical IS curve and a horizontal LM curve, i.e. a particular case for an economy but not for an economy in all possible scenarios. In such a case his theory would not be universal, as we try to portray it.

Keynes developed his general theory in times of the great economic crises when there was need to explain why and how can it happen that the monetary policy is inefficient. These are cases when the LM curve is horizontal or almost horizontal and when only fiscal policy is efficient, if we stay within the IS-LM framework. In times of economic crises no proper expansionary monetary policy was conducted, and thus there is no empirical evidence of its inefficiency. Correlation between the quantity of money or its reduction, and the level of national income or its reduction was large. Because the quantity of money was decreasing, Keynes' opponents use this fact as evidence for validity of the quantity theory of money. Banks were going bankrupt as in that time there was no mechanism to prevent it, which lead to a decreasing volume of bank loans and quantity of money. Inefficiency of monetary policy would

[6] According to D. Patinkin the problem of empirical verification is the existence of a very good correlation between views which politics to conduct and empirical results (Patinkin, 1972, p. 142).

show if, hypothetically, the central bank conducted expansive monetary policy to try to move the LM curve to the right. Because of corporate bankruptcies, increasing unemployment and decreasing aggregate demand the IS curve was moving to the left, and thus moving the LM curve to the right would not prevent the fall in national income. Under these conditions fiscal policy is efficient and monetary policy is inefficient. However, this can change. In the IS-LM diagram as presented by Keynes, IS and LM curves can intersect at a point where the LM curve is not near horizontal but on the contrary near vertical. In such a case, monetary policy is efficient and fiscal policy is not.

4. IS-LM diagram in an open economy

Openness of the economy and international mobility of capital are important for small economies. Openness of the economy was not incorporated in the original IS-LM as this issue was not important at that time. In light of rapid financial development and an increasing number of financial assets, many of them very liquid, it became important whether money, i.e. the so-called "narrow money", adequately represents liquidity. It is well known that for central banks the so-called "broad money" or M3 is more important. Many central banks replaced the instrument of quantity of money with interest rates, the meaning of which is clearer. But let us leave this aside for the moment.

In order to study transition economies, we need to add the balance of payments curve (BP) to the IS-LM diagram. We arrive at the Mundell-Fleming diagram.[7] In this diagram the IS curve reflects the equilibrium between, on the one hand, the sum of investments (I) and exports (X), and on the other hand the sum of savings (S) and exports (M). This ISXM curve has the same shape as the IS curve for a closed economy, but its slope is steeper.

The LM curve remains unchanged. The BP curve shows combinations between the national income (Y) and interest rate (i), where the balance of the current account of the balance of payments equals the balance of capital transactions, but with the opposite sign, and therefore the international reserves remain unchanged. In the current account of the balance of payments exports are exogenous and imports depend on the level of the national income. The BP curve runs from the low left corner of the diagram with Y and I, towards the upper right corner. If the international mobility of capital is perfect, then the BP curve is horizontal at the interest rate determined

[7] The Mundell-Fleming model by J. M. Flemingom (Fleming, 1962) and R. A. Mundellom (Mundell, 1963). According to V. Argy (Argy, p. 53), it is an extension of the IS-LM model to include open e economies. This, of course, does not imply that Fleming and Mundell were Keynesians.

by international financial markets. With no international mobility of capital, the BP curve is vertical at level of national income which reflects the external equilibrium.

When analysing transition we shall not consider the extreme positions of the IS, LM and BP curves. We are interested in general how to use the IS-LM curve of an open economy to show and/or explain economic problems of transition countries. With economic problems of transition we mean the key or basic problem at the start of transition, i.e. the abolition of state ownership of companies, or in the case of the former Yugoslavia, the abolition of social ownership of non-financial enterprises. Market economy cannot be introduced with non-financial enterprises being socially owned.

5. How to abolish state or social ownership of enterprises

It is well known that Keynes saw all followers of the Say law as economists of the classic school. All of them were on the other side and he criticised them. The transition and the need to abolish state or social ownership gave rise to the question of how to sell the existing assets, for instance non-financial enterprises. This can be done following the example of non-transition countries. However, in transition countries supply does not automatically create demand. In general, selling existing assets within a country is not a problem because domestic owners merely swap assets. Some are selling and some are buying. Each sale is at the same time a buy. After transactions have been completed, merely the distribution of assets among residents has changed, and the assets are still owned by residents. The private sector has no need for additional funds or equity, which result from savings.

When abolishing the social ownership of non-financial enterprises the key problem is that residents, who have not been owners before, have to become the new owners. For a moment we disregard foreign investors, which we will include later. If residents become owners of companies, we have a re-distribution of assets among private persons and the government or society. But something else is of greater importance to us. This is not merely a different distribution of assets among domestic private sectors. On the left side of the balance sheet of the private sector (individuals and legal entities) there is a new item, ownership of enterprises, for example in the form of shares. Due to the logic of balance sheet, this must result in a decrease of something else on the left side of the balance sheet, or the right side (equity) has to grow. As we know, the latter can grow only through savings.

During the '90s privatisation in Western countries the government was buying back its bonds to enable the private sector to buy companies. Hence, for the private sector the privatisation was merely a change of the composition of its assets. Instead of government bonds they received private companies. As in transition economies the

private sector at the beginning of privatisation did not have government bonds, this approach could not have been applied. We needed a different solution. However, as we did not want to find the right solution, we found a wrong one. Shares in companies were distributed to residents for free and/or were sold to domestic and foreign entities at the market price, as argued at that time. All this was logical, market oriented and fair.

These two methods, i.e. distribution of shares to residents and sale of shared to residents or investors, can be very different in some aspects. Distribution of shares is preferred by residents and is politically appealing. Both methods however come down to the same issue is we look at macroeconomic consequences, for example the effect on savings and thus on the formation of the domestic capital. We arrive at a decline of savings (I) and/or an increase of consumption. The IS curve in the IS-LM diagram moves to the right (charts 1 and 2). If assets distribution is fair, after a short period of time, usually after the expiration of sale restrictions, most residents sell their shares. They are bought by a small group of domestic legal entities with money or assets created by savings, and this money will be spent by sellers of shares to increase their consumption. This brings us to a decline in savings (S) and/or an increase in consumption (C) in the national economy. If shares are not distributed for free to residents but are sold to those offering the highest price, the private sector uses its savings for buying existing assets. These, of course, are not savings from the national economy's point of view.

The question remains how the money paid by residents for shares in former socially owned enterprises is used. If it is spent for investments in the economy by the government, then we do not have a privatisation. If the money goes into the budget and consequently the government lowers taxes, consumption (C) will increase. The third option is the government spending privatisation proceeds for investments abroad. It becomes the owners of assets abroad, a kind of compensation for giving up ownership of enterprises at home. In this case domestic savings (S) remained unchanged. In the IS-LM diagram the BP curve moves up and/or to the left because of a smaller net import of capital. Of these three possible scenarios for spending privatisation proceeds the only "clean" or straightforward option is a reduction of taxes. With the other two options the government keeps ownership of assets either at home or abroad. Government assets do not decrease. In this case we observe a reduction of savings (S) or an increase of consumption (C), i.e. a move of the IS curve to the right.

If the government sells companies to foreign investors, there is first an inflow of foreign money to the foreign exchange market. The BP curve moves down and/or to the right. The consequences depend, as we will see, on what the government will do with the money and how the central bank will react. We can draw some conclusions. If the government does not repurchase its bonds from the domestic private sector to enable the private sector to buy companies put for sale by the same government,

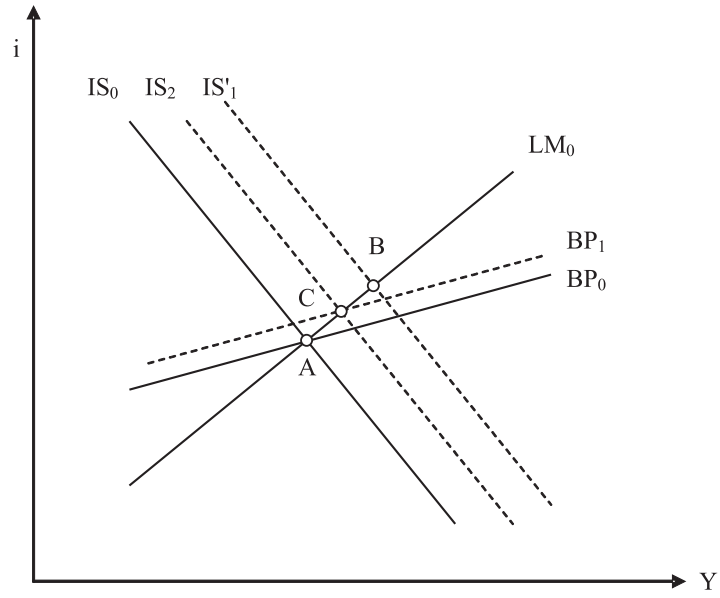
and if the government in the case of selling companies to foreign investors does not compensate this sale by reducing foreign debt, there will be negative consequences for the economy. Let us see whether the IS-LM diagram can help understand these developments, of course ex post, although these issues had been raised at the time (Ribnikar, 1993 and Ribnikar, 1994).

6. The abolition of social ownership of non-financial enterprises via distribution of shares to residents and/or sale to domestic entities

As already indicated above, if shares are distributed to residents they will, after some time, start selling them to a small group of people. This leads to a decrease of savings and to the IS_o curve moving to the right (Chart 1). The outcome is similar to that of companies being sold to domestic entities and taxes being reduced. The effects on the reduction of savings are probably somewhat smaller. The new curve is IS_1. This brings us to point B in Chart 1, which shows the external equilibrium. The current account of the balance of payments is deteriorating, but the increase in interest rates leads to increased capital import. This additional import of capital is larger than the deterioration of the current account of the balance of payments, resulting in balance of payments surplus. The central bank can prevent domestic currency appreciation by sterilising purchases of foreign exchange surpluses in the foreign exchange market. The economy stays in point B. However, the central bank can only do this for a limited period of time. Evidence from different countries shows that this can be some years.

Foreign currency depreciates if the central bank does not undertake sterilized market interventions in the foreign exchange market to prevent it. The BP_o curve moves upwards to the BP_1 curve. Simultaneously because of domestic currency appreciation the IS_1 curve moves leftwards to IS_2. The new equilibrium is in point C. Comparing points B and C we can see that the current account of the balance of payments deteriorates more in point C. In point C the current account of the balance of payments deteriorates and the exchange rate decreases – for instance the German mark.

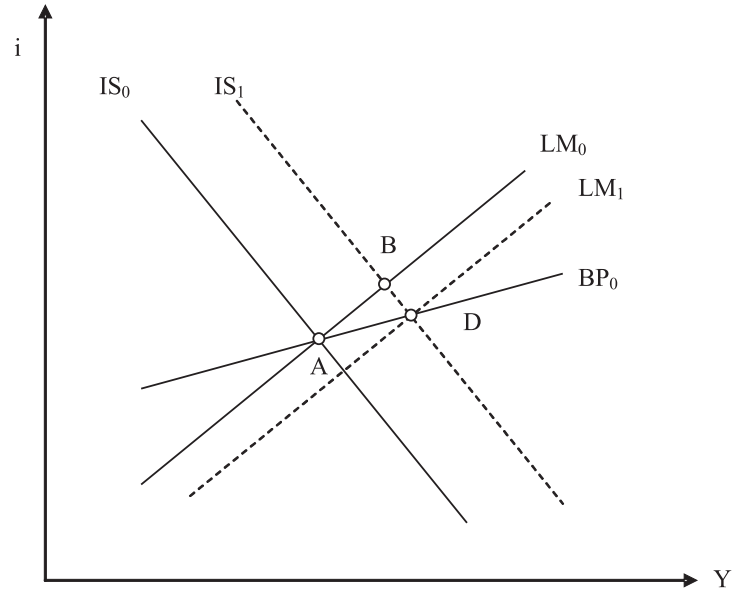
Chart 1: The effect of a decrease in savings (moving the IS_o curve to the right) with the central bank undertaking sterilising purchases of foreign currency (point B) and with a floating exchange rate regime (point C)



Sources: Author

The central bank can also opt for non-sterilising purchasing of foreign currency surplus (Chart 2). The central bank has to purchase these surpluses because, for example, it runs a fixed exchange rate regime. This leads to monetary expansion with the LM_o curve moving to the right towards LM_1, establishing a new equilibrium in point D. In contrast to point B, here we are probably facing inflationary pressure (from the chart we cannot see what is happening with prices). The deficit of the current account of the balance of payments is larger in point D than in point B because of a lager national income (Y).

Chart 2: The effect of a decrease in savings (moving the IS_o curve to the right) in a fixed exchange rate regime, supported by the central bank undertaking non-sterilising purchases of foreign currency surplus



Sources: Author

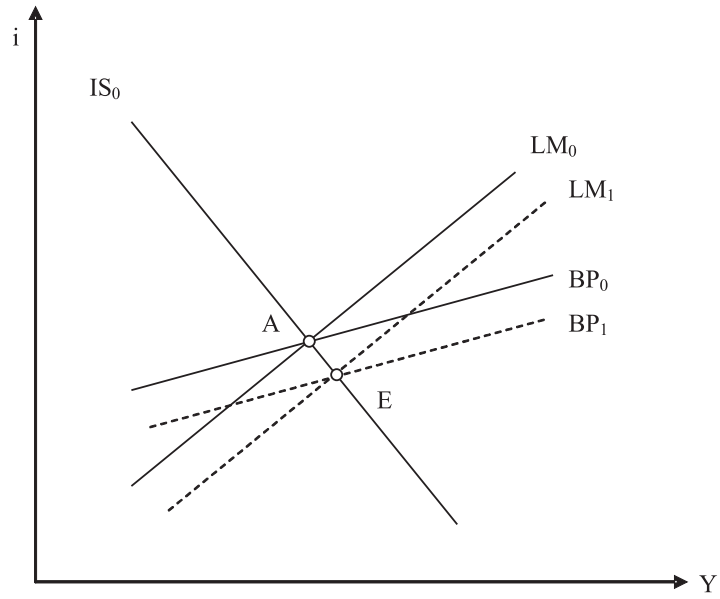
Let us compare the three possible equilibria, i.e. point B (Charts 1 and 2), point C (Chart 1) and point D (Chart 2). In case of social ownership abolition where we face a reduction of savings, the central bank should undertake sterilising purchases of foreign currency to prevent appreciation of the domestic currency. If the central bank cannot or does not want to do it, then we face either monetary expansion (point D) or appreciation of domestic currency (point C).

7. Abolition of social ownership of non-financial enterprises by sale to foreign investors

In case of a sale of enterprises to foreigners the BP curve moves downwards because of the inflow of money into the country and the excess supply of foreign currency. We get from the BP_o curve to the BP_1 (Chart 3), and point A does not anymore show the external equilibrium but a balance of payments surplus. As a consequence of sale to foreign investors, additional foreign currency is flowing into the foreign exchange market. If the central bank wants to prevent depreciation of foreign currency (euro), it has to buy the excess foreign currency. If it undertakes sterilising purchases, nei-

ther the quantity of money nor the exchange rate change. We stay in point A, now showing external disequilibrium.

Chart 3: The effect of selling enterprises to foreign investors with sterilising (point A) and non-sterilising purchases (point E) of excess foreign currency by the central bank.

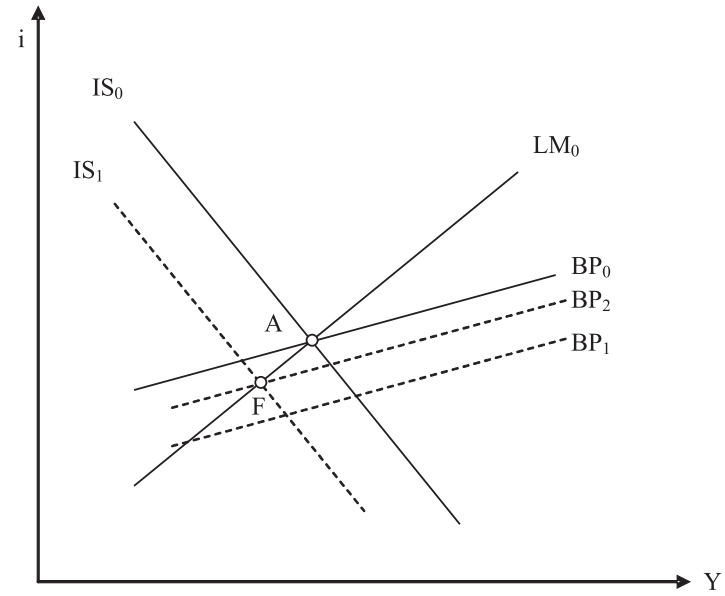


Sources: Author

Even in the case of large foreign currency inflow and non-sterilising purchases, the central bank can keep the exchange rate unchanged. The result is monetary expansion, i.e. the LM curve moving to the right and/or downwards. From the LM_o curve we get to the LM_1 curve and to the new equilibrium (point E in Chart 3). This point shows, because of the monetary expansion, larger deficit of the current account of the balance of payments and probably inflation.

There is a third scenario. The central bank can allow the exchange rate to adapt to the increased inflow of money into the country. It can allow depreciation of the exchange rate or appreciation of the domestic currency (Chart 4). The central bank does not intervene in the foreign exchange market. In this case the BP curve moves upwards from BP_1 to BP_2. In addition, the IS curve moves to the left. Moving from the IS_o curve to IS_1 we arrive in the new equilibrium point F (Chart 4).

Chart 4: The effect of selling enterprises to foreign investors in a floating exchange rate regime



Sources: Author

In point F we have, because of appreciation of the domestic currency, a larger deficit of the current account of the balance of payments that in point A. The deficit of the current account of the balance of payments is financed with money from selling enterprises to foreign investors. If we compare the three possible equilibria, i.e. point A (Charts 3 and 4), which is not a long term equilibrium, point E (Chart 3) and point F (Chart 4), we arrive at similar conclusions as we did in the case of selling enterprises to domestic entities or distribution of shares to residents. From an economics point of view the best solution is if the central bank prevents appreciation of domestic currency by undertaking sterilisation purchases of foreign currency, and hence prevents monetary expansion. This is the case in point A, which shows external imbalance and therefore is not sustainable in the long or very long term. If the central bank does not choose this option, then it has to choose between monetary expansion and probable inflation, if it keeps the exchange rate unchanged by undertaking non-sterilising purchases of foreign currency (point E), and appreciation of domestic currency, if it does not intervene in the foreign exchange market (point F).

But, in the end, we are interested whether it would be possible to choose less unfavourable effects, i.e. cases depicted by point A in Chart 3 and point B in Chart 1. Let us take a look at a scenario of social ownership abolition through transferring of shares of non-financial enterprises to a pension fund or several pension funds.

However, it is not sufficient if a pension fund becomes the owner of shares. Proper legislation regulating the fund's operations must to be in place.

The fund would have to use the proceeds from selling shares of enterprises to residents for buying domestic bonds, both government and private. When selling shares to foreign investors, the fund should perform compensatory purchases of foreign bonds or equity. If the pension fund performs compensatory purchases of domestic bonds, only the composition of assets of domestic private sectors changes. If the fund sells shares of enterprises to foreign investors and performs compensatory purchases of foreign bonds and equity, there is no import of capital and therefore no need for the central bank to undertake sterilising or non-sterilising purchases of excess foreign currency because there are none. The economy stays in point A with the three equilibria.

Let us come back to compensatory purchases of domestic bonds. The limited supply of these papers could pose a problem. The best option, of course, would be to limit the sale to residents to an amount equivalent to the potential compensatory purchases of domestic bonds (and other debt obligations). If this is not possible because there are no domestic bonds available, and a delay in selling shares of enterprises is not an option, pension funds have to buy foreign papers. The economy would not stay in point A in Charts 3 and 4. The BP curve would move upwards and/or to the left. Point A would show a balance of payments deficit. The money would be flowing abroad. The best option would be for the central bank to intervene by sterilising sales of foreign currency to prevent the simultaneous appreciation of foreign currency and monetary contraction.

If the abolition of social ownership is done through transfer of enterprises to a pension fund, a subsequent sale of these enterprises to domestic and/or foreign private entities by the pension fund would be the same as privatisation of companies in non-transition economies. The only difference would be that in non-transition economies the government would be buying back from the private sector its bonds to prevent negative consequences to savings (S). In the former Yugoslavia with social ownership of non-financial enterprises this function would be carried out by the pension fund. The pension fund would compensate the sale of enterprises to domestic entities by buying domestic bonds (private and government), and the sale of enterprises to foreign investors by buying foreign bonds and shares.

8. Conclusion

In the paper we were interested primarily in two issues. First, is there a problem of how to privatise or abolish social ownership of non-financial enterprises, taking into account the specificity of the former Yugoslavia, where all or almost all enterprises had been in social ownership and had to be transferred into private hands. Can this

be done in a very simple manner by selling and/or distributing shares to residents? When non-transition countries, at a much smaller scale, privatised state companies the government realised that it had to assist the private sector to enable it to buy the companies. The government was in parallel selling state owned companies to the private sector and buying back government bonds from the private sector. This was then source of funds the private sector needed for the privatisation. In transition countries, however, this was "forgotten" by governments and their privatisation consultants. We showed how the government should have solved this problem in transition economies where the private sector did not hold government bonds to sell them back to the government in order for residents to secure funds to buy shares in companies. In a way this problem is similar to Say's law.

Second, we were interested in the central bank, i.e. its monetary policy and foreign exchange rate policy. We showed that the role of the central bank is particularly important when the government does not provide conditions for a painless privatisation or painless abolition of social ownership. By painless we mean without negative or adverse consequences for domestic savings and formation of domestic capital. We know that these conditions were not fulfilled, and the best or the least bad option is for the central bank not to allow monetary expansion and consequently appreciation of the domestic currency. The central bank can prevent it by undertaking sterilising interventions in the foreign exchange market.

The dimensions and other characteristics of the challenge faced by transition countries were not know. We saw some of the characteristics, for instance the inexistence of government bonds in possession of the private sector. Because of that the solution could not be found in models, theories or directly in the real world experience of non-transition economies. The link to Keynes or Keynesianism is not in first place his diagram, which we used to explain or better illustrate problems of transition economies at the beginning of transition towards market economies, i.e. how to get to private ownership of companies, but the connection in the sense that the transition cannot be done in a simple way with all problems solved by market forces. We showed what the government or its central bank should have done to render the transition to market economy economically, socially and morally less painful. Countries with less confidence in market forces probably fared better.

J. Attali, who in his younger days never studied Marx and is not a Marxist, in his biography labels Marx as the ghost of today's global world (Attali, 2005). Marxist M. Desai shares a similar view (Desai, 2002). Marx anticipated today's global world and he would, in a way, have gladly accepted it. It cannot be very uncommon if Keynes or ideas stemming from his theories are relevant for today's transition economies. [8]

[8] According to P. Fitoussi (Predet, 2006), E. Phelps for example is convinced that the market cannot lead to an acceptable equilibrium. The role of the government is very important, however not in the form as perceived by the "keynésianisme simpliste".

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Keynesova monetarna teorija i tranzicijske ekonomije

Ivan Ribnikar[1]

Sažetak

Nakon kratkog pregleda o čitanosti, diskusijama i prihvaćanju Keynesove monetarne teorije prije nastupanja tranzicijskog procesa početkom devedesetih godina prošlog stoljeća, u radu se analiziraju dva ključna problema. Prvi se odnosi na prodaju poduzeća, odnosno na izdavanje i prodaju dionica u tranzicijskim zemljama, budući da su organizacije bile podvrgnute transformaciji iz društvenog vlasništva u privatni sektor dioničkih društava i društva s ograničenom odgovornošću. Drugi problem koji se razmatra odnosi se na centralnu banku i ulogu koju bi trebala odigrati – osobito u situacijama kad vlada nije omogućila domaćem privatnom sektoru kupnju poduzeća. Centralna banka treba spriječiti bilo monetarnu ekspanziju bilo aprecijaciju domaće valute pomoću sterilizacijskih kupovina viškova deviza na deviznom tržištu. Oba problema su na neki način povezana s Keynesovom teorijom i/ili ekonomistima poslije njega bilo da su bili ili ne bili njegovi sljedbenici.

Ključne riječi: *monetarna teorija, Keynes, tranzicijske zemlje, IS-LM dijagram*

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